FILE COPY

IN THE

Supreme Court of the United States

No. 757

October Term, 1937

The United States of America,
Appellant,

v.

Milo W. Bekins and
Reed J. Bekins, as Trustees appointed by the Will of
Martin Bekins, deceased, et al.

BRIEF AS AMICI CURIAE IN SUPPORT OF APPELLANT

Cary D. Landis,
Attorney General of Florida.
Giles J. Patterson,
Special Counsel.

INDEX AND SUMMARY

Brief of Cary D. Landis, Attorney General of Florida and Giles J. Patterson as Amici Curiae.

ARGUMENT

CITATIONS

IN THE

Supreme Court of the United States

No. 757

OCTOBER TERM, 1937

THE UNITED STATES OF AMERICA,
Appellant,

v.

MILO W. BEKINS and
REED J. BEKINS, as Trustees appointed by the Will of
Martin Bekins, deceased, et al.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR
THE SOUTHERN DISTRICT OF CALIFORNIA,
NORTHERN DIVISION.

BRIEF OF AMICUS CURIAE

This brief being filed by Amicus Curiae will not attempt a statement of the case. It is confined solely to a discussion of the constitutionality of the st..ute. As the decision

of the District Judge that the statute is unconstitutional rested solely upon his conclusion that the present act could not be distinguished in point of substance from the Act of Congress held void in the case of Ashton v. Cameron District, etc., we shall confine the brief narrowly to a discussion of this one point. It is our position that H. R. 5969 is not subject to the condemnation that was visited by the Supreme Court upon Chapter 186 of April 10, 1936. In fact, we submit that it can be almost mathematically demonstrated that the present statute not only was drawn in the light of that decision and eliminated the unconstitutional features of that act, but that the changes made in the act are substantial, material and vital, and eliminate any possible interference with the sovereign power of taxation of a State or with any taxing district's control over its fiscal affairs.

We assume for the purpose of this discussion the correctness of the reasoning of the majority opinion in Ashton v. Cameron County Water Improvement District No. 1, 298 U. S. 513, and also its conclusion that the former statute "might materially restrict the district's control over its fiscal affairs and was therefore void." We also assume as a predicate, the admission in both the majority and minority opinions that the former statute was "adequately related to the general subject of bankruptcy." In this way the legal argument herewith presented is confined to a narrow issue. In order to present it we therefore submit:

1. That the purpose and intent of Congress was to enact a statute that was different from the one held void.
2. That the present statute differs in material particulars from the act held void.
3. That these differences are vital, fundamental and far-reaching and eliminate entirely the reason given by the Supreme Court for holding the former act unconstitutional.

FIRST

That the Purpose and Intent of Congress was to Enact a Statute That was Different From the One Held Void.

The brief of the government refers to the decision of this Court in Wright v. Vinton Branch 300, U. S. 440, 81 L. Ed. 736, and to the report of the Judiciary Committee of the House, Pages 76 and 77. The testimony that was taken at the hearing before the Sub-committee of the Judiciary Committee of the House of Representatives, especially statements of Mr. Wilcox, author of the act, on pages 128 and 129, support the conclusions of the committee.

SECOND

That the Present Statute Differs in Many Material Particulars From the Act Held Void.

The distinction between the present statute and Section 80, which was held void, is apparent from the differences in terminology and in form. Section 79 of the former act provided that in addition to the jurisdiction in bankruptcy the court should

> "exercise original jurisdiction in proceedings for the relief of debtors as provided in this chapter of this title."

Section 80 and its various subdivisions follow in a general way the provisions of Section 77 (a) and 77 (b) relating to railroad and general corporate reorganizations and readjustments. In Sub-section (a) of Section 80 the proceeding, when filed, is referred to as a petition to "effect a plan of readjustment of its debts." Throughout the statute the words "Plan of Readjustment" are repeatedly used. Such a plan under Sub-section (b), Section 80, might

include provisions "modifying or altering the rights of creditors generally" or, any class of them secured or unsecured, either through the issues of new securities of any character or otherwise, and might contain such other agreements and provisions not inconsistent with the chapter as the parties desired. Sub-section (c), which dealt with procedure also differed materially from the present statute. It authorized the Judge to require the district to file

> "such schedules and submit such other information as may be necessary to disclose the conduct of the affairs of the taxing district and the fairness of any proposed plan."

It authorized the rejection in whole or in part of executory contracts. It required the taxing district to open its books for inspection by creditors, and that,

> "the taxing district shall be heard on all questions."

Sub-section (e) authorized changes and modifications of the plan of readjustment and Sub-section (g) relieved the district "from debts and liabilities dealt with in the plan except as provided in the plan." When these broad provisions are read in connection with Sections 77 (a) and 77 (b), the statement of Justice McReynolds in the majority opinion in Ashton vs. Cameron County that,

> "our special concern is with the existence of the power claimed—not merely the immediate outcome of what has already been attempted. And it is of the first importance that due attention be given to the results which might be brought about by the exercise of such a power in the future,"

assumes greater importance. We interpret this as laying stress more upon what the statute might be construed to authorize in other cases than upon the particular purpose sought to be accomplished in the case then before the court.

The present statute avoids the use of these broad and sweeping provisions and, while it is reminiscent of the form of Section 80, it is patterned more after Section 30, Title 11, U. S. C. A., than after Section 77 (a) and 77 (b). Illustrative of this fact is the use of the word "composition". The first sentence of Section 81, gives a court of bankruptcy jurisdiction "for the composition of indebtedness of or authorized by any of the taxing agencies or instrumentalities" therein named. The term "composition" is used throughout the entire statute.

Admittedly a change in terminology is not controlling but should be considered in connection with the purpose of the authors of the act. The word "composition" has come to have a very definite meaning as applied to proceedings in bankruptcy courts. It was first adopted in England and later became a part of the National Bankruptcy Act of 1874. It was included in the Bankruptcy Act of 1898 as amended by Chapter 412, Acts of June 25, 1910. The phrase "Plan of Readjustment" was first used in Sections 77 and 77 (b) and its meaning is necessarily associated with proceedings under those sections in the same way that the meaning of the word "composition" is associated with proceedings under Section 30, Title 11. Terminology in a statute is always important when we seek to construe its meaning and purpose, unless the effect of the statute be inconsistent with the terminology employed.

The effect of a "composition" in bankruptcy and the validity of the statute authorizing compositions has been repeatedly before the courts, and its extent is well defined.

Section 80 was subject also to the claim that under it the court was authorized to pass upon the Plan of Readjustment. Although the phraseology of sub-section (e), Section 80, is similar to that of subdivision (e) of Section 83, yet when read in connection with subdivision (c) of Section 80, which authorized the court to require the district to file schedules and submit other information to disclose the conduct of its affairs and the "fairness of any proposed plan",

it appeared that the court was authorized to determine the ability of the district to pay its creditors, and to refuse to approve a plan, if on its face it appeared that the district was offering less than it was able to pay. The requirement that the plan should be a fair one is analagous to the construction which the Federal Courts had placed upon the present Frazier-Lemke Act requiring that the plan shall be in good faith. The construction of this language requires a plan reasonably calculated to effect the liquidation of the debt. Section 83 omits the provision for filing schedules to show the fairness of the plan. Its fairness is to be determined as the fairness of compositions offered under Section 30, Title 11.

Another vital distinction between the two statutes appears in sub-section (a), Section 80, as applied to drainage districts, reclamation and levee districts. In such district the act required the consent of only 30% of the creditors in order to file a petition. Compositions inherently arise only from the agreement between the debtor and a majority of its creditors.

Section 83 requires the written consent of a majority in amount in drainage districts as in all other cases.

Another essential difference between the two statutes is found in sub-section (c), Section 80, which authorizes the court by interlocutory decree to declare the plan temporarily operative and to authorize postponement or extension or readjustment of the payment of principal or interest in the manner proposed in the plan, as well as to stay *all pending suits* until after the final decree. Section 83 conditions this authority by saying that it shall not apply "where rights have become vested". This exception, while apparently small, expressly protects the rights of persons holding judgments upon which a preemptory writ of mandamus has been issued, who in United States v. Brown, are held to have acquired vested rights. Since neither statute contemplates the appointment of a Trustee in Bankruptcy to recover preferences, the distinction is important. A plan of read-

justment would contemplate taking away from creditors rights which had become vested. Under the present statute such rights are not interfered with. The distinction made by the Supreme Court in Wright v. Vinton, supra, between the original Frazier-Lemke Act and the amended act illustrate the importance which this court attaches to the protection of vested rights, even in a bankruptcy statute. The fact that the statute does not expressly describe vested rights is not material. In Louisville Joint Stock Land Bank v. Radford, this court held that a bankruptcy statute could not deprive mortgagees of their vested rights, but in Wright v. Vinton, supra, the amended act was held valid because it did not attempt to do so.

Probably the most important difference between Section 80 and Section 83 is found in the provisions of sub-section (f) of the present statute. No such provision was contained in Section 80. The court can enter only an interlocutory decree of confirmation until the debtor shall have deposited with the court, or, with such disbursing agent as the court may appoint or otherwise made available to its creditors, the moneys, securities or other consideration to be delivered to the creditors under the terms of the composition. The bankruptcy statutes have always required the consideration for the composition to be deposited in the court. Under Section 80 the court might find itself unable to enforce the plan of readjustment even after the taxing district and the creditors had complied with the terms of the statute and final decree of confirmation had been entered. There was no way in which the district court could compel the taxing district to carry out the terms of the Plan of Readjustment which had been approved. If the statute had been construed to compel compliance with the plan by the taxing district an order requiring the same would have clearly infringed the power of the State to control its own political subdivision. It would have been in the nature of an order for specific performance effective only by mandatory decree. As the Plan of Readjustment contemplated the issue of new

securities, the court would have had to require the passage of resolutions necessary to authorize their issue, the printing, signing and sealing of the same, as well as the delivery of them. Such order would have clearly controlled the powers of government of the local community. The act in such a situation would have permitted the Federal Court to interfere with the taxing district's management of its own fiscal affairs. Under the present statute no such situation can arise. The order finally confirming composition cannot be made until the securities, moneys or other consideration for the composition has been placed under the control of the District Judge. He can make distribution of them to the creditors and thus render the final decree conclusive against the rights of all creditors. The court itself can deliver to those who have accepted the composition their proportional part and hold for the account of those who have not accepted the proportion which they are entitled to receive.

This deposit of the consideration for the composition gives to the court the rem and renders the act analagous to all bankruptcy, admiralty and other statutes where the jurisdiction of the court depends upon the court's possession of the rem. In fact, jurisdiction of bankruptcy proceedings generally is sustained largely upon possession of the rem which it can distribute. A discharge in bankruptcy does not affect the rights of creditors, but merely the remedies which they possess.

Next, let us consider whether the statute differs from Section 30. First, it differs to the extent that no final decree of adjudication of bankruptcy and sale of assets can be made. Thus much is admitted. Second, it requires the consent and acceptance by a majority of all creditors rather than a majority in number and amount. Third, the offer of composition is made and accepted before the petition is filed. Fourth, under the Uniform Act a composition can be offered only after the bankrupt has been examined in court. None of these differences relate to the constitu-

nal question here considered, unless it be assumed that cause an adjudication in bankruptcy cannot be entered, proceeding for composition is not a statute relating to nkruptcy.

The majority opinion in the Ashton case held the statute a whole unconstitutional; and not because of any spe- c provision. The majority opinion said that it was not cessary "to consider the act in detail as the evident in- t of it was to authorize the Federal Court to require the jecting creditors of a public corporation to compromise, le down or repudiate its indebtedness without surrender the debtor of its property." It held further Section 8, ticle I, of the Constitution of the United States

> "is impliedly limited by the necessity for preserving the independence of the States."

at,

> "its (the taxing district's) fiscal affairs or those of the State, not subject to control or interference by the National Government, unless the right so to do is definitely accorded by the Federal Constitution."

d, concluded that

> "as application of the statutory provisions now before us might materially restrict respondent's control over its fiscal affairs"

trial court rightly declared the statute invalid.

The purpose of the present statute and its provisions initely and conclusively show that under no circum- nces does it authorize a Federal Court to control or in- fere with the fiscal affairs of districts and that the oper- on of the statute can in no sense of the word impinge on or affect in the slightest degree the independence of tate or the exercise either by the State or its taxing ricts of the sovereign power of taxation.

The fact that the statute does compel objecting creditors to compromise, scale down or repudiate the indebtedness owing to them and that such may be compelled even "without surrender of property" by the municipality, is of no consequence as such is the effect of Section 30, Title 11, of the Uniform Bankruptcy statute upon the debts of individuals.

It is our contention therefore that even if the former act was subject to criticisms made of it, the present statute is not subject to the same infirmities. The brief filed by the government, pages 25-33, reviews the history of bankruptcy legislation and the statutes which this court has held come within the meaning of the constitutional power of Congress. Hanover National Bank v. Moyses, 186 U. S. 181. This court in its opinion in the Ashton case assumed that the act there considered related to the subject of bankruptcies. Even assuming that it did, it was held unconstitutional because it might have authorized Federal Courts to interfere with the independence of State authorities and the exercise by the State and its subdivisions of their powers. The authors of the present act in drafting the same therefore have assumed that if this statute does not interfere with the State's sovereign power of taxation or the management by the local subdivision of its own fiscal affairs, it is valid in the absence of other constitutional defects. It is necessary here to anticipate a claim that Section 8 was ipso facto not intended to apply to taxing districts, merely because it had never been applied. The fact that Congress has not heretofore extended bankruptcy statutes to State taxing districts is explained by the fact that conditions have not heretofore warranted such an extension. As Section 8 authorizes statutes relating to bankruptcy, any statute which relates thereto and does not violate some other provision of the Constitution, express or implied, such as the implied limitation arising out of the dual form of government, is necessarily valid.

The Differences Between Section 80 and Section 83 Are Fundamental.

The very theory of a composition as it has been outlined by this court and the Courts of Appeals, especially in the opinions of the latter which have been cited with approval and quoted in decisions of this court, contemplates the settlement, compromise or scaling down of debts as a result of an agreement or contract between the debtor and the majority of its creditors. It contemplates retention by the debtor of the possession of his estate. A court in approving a composition is not concerned with the amount of the consideration so long as there is no discrimination between creditors of the same class; no special inducements are offered creditors to consent, and no fraud is practiced by the debtor or consenting creditors upon the non-consenting. The consideration for the composition need not consist solely of cash, but may be represented in new notes, secured or unsecured, stock or other evidences of indebtedness. The consideration must be deposited with the court and held by it for the benefit not only of consenting creditors but of the dissenting creditors as well upon a pro rata basis. When confirmed the debtor is discharged to the same extent as he would be by an adjudication and discharge may be pleaded as a release against any subsequent action brought upon the original obligations. In fact, this court has repeatedly held that a composition "originates in a voluntary offer by the bankrupt, and results in the main, from volutary acceptance by his creditors." Nassau Smelting & Refining Works v. Brightwood Bronze Foundry Company, 265 U. S. 267, 68 L. Ed. 1013. That

> "the will of the majority of creditors is enforced upon the minority provided the decision of the majority is approved by the court, except for this coercion of the minority the interference of a court of bankruptcy would hardly be necessary."

And again it said

> "it is a proceeding voluntary on both sides by which a debtor of his own motion offers to pay his creditors a certain percentage of their claims in exchange for release from his liabilities. The amount there may be less or more than would be realized from distribution in bankruptcy."

The effect of the composition proceeding is to substitute the composition for bankruptcy, and in a measure to supersede the latter proceeding and to reinvest the bankrupt with all of his property free from the claims of his creditors.

In Re Reiman v. Freedlander, Federal Case 11673, decided under the statute of 1867 authorizing a composition, sustained the validity of such section, because the composition accomplished the end of bankruptcy, namely, "a substantial appropriation of the existing property of the debtor towards all the debts due by him," and because the proceedings provided for "a pro rata payment on the debts (not) only of those creditors who proved their debts, but of all creditors ought to have a payment pro rata." A composition restores to the bankrupt his estate and frees him from all of his debts, reinvesting title to his property in him. When a composition is confirmed, jurisdiction and control of the bankruptcy court ceases, unless expressly retained for the purpose of carrying out special terms of the composition, or to the extent it may be necessary to restore to the bankrupt any assets taken from him. The present statute, Sec. 83, leaves the debtor in possession of its assets. By its terms it releases the debtor from liability on its original debts and upon the distribution of the consideration by the court its jurisdiction terminates. Final decree is binding upon all creditors who have not filed, as well as upon those who have. Sub-section (f.) Remington on Bankruptcy, Vol. 7, 1934, Edition, Section 3092, says that it was the intention of Congress to make it possible for the bankrupt to obtain a composition "on the strength of depositing something else than money". The Circuit Court

Appeals in Kinkead v. J. Bacon & Sons, 230 Fed. 362,
d that consideration for a composition

> "may or may not be cash. A bankrupt usually does not have enough ready money of his own to carry out a composition. The consideration to be paid may be the bankrupt's notes, secured or even unsecured, or his mere promise to pay in the future a given amount." Citing 2 Loveland on Bankruptcy (4th Ed), p. 1264. See also In Re Kinnane (D. C.), 221 Fed. 762.

Not only does the statute not interfere with the State's wer of taxation or the power of a local taxing district to nage is own affairs, but it actually makes it possible for district to manage its own affairs. The condition which fronts cities, towns and other taxing districts, whose in-btedness is in default, principal or interest or both in large ns, is not necessarily an inability to pay ultimately, but inability to meet its obligations currently. In order to y its debts properly it must have time and it must be able maintain its governmental functions, otherwise its ability collect taxes in the future will be definitely impaired. rticularly is it important to realize that there is no limi-ión upon the amount of tax that can be levied, either governmental purposes or for the payment of debts, un-s the statute imposes specific limitations. With an un-ited power of taxation pledged for the payment of debts l the necessity for exorbitant annual recurring levies re-ting from an accumulation of past due obligations, pled with the necessity which confronts a taxing dis-ct which is required by writs of mandamus to levy taxes them, even though such writs be tempered by a distribu-n of over a period of years—the district soon finds itself ble to collect them. When the tax is out of all propor-n to the ability of property to respond, the district is ble to meet even its necessary recurring charges for gov-mental purposes. The writs require the performance of ditions which in their very nature are impossible. This tute permits the taxing district to arrange its affairs in

an orderly fashion by postponing the maturity of interest or principal, or both, and permits it to take advantage of lower interest rates which the majority of its creditors agree to accept because of local conditions or because the prevailing rate is lower. It furnishes a practical and useful vehicle that will help to preserve the integrity of local governments. It will prevent situations like those which occurred in the middle west, where debts remain unpaid for thirty and forty years. Meanwhile the counties and cities found it impossible to perform their governmental functions. The fact that the statute may authorize a reduction even in principal does not differentiate it from other compositions under Section 30. In fact, this is its very purpose.

The acceptance of a composition provided a sense of security to property owners against confiscation of their property under exorbitant tax levies. This cannot be furnished in any other way. In fact, a composition carried through will necessarily in time reestablish the credit of local subdivision and enable it to borrow money to meet its future needs. The history of other subdivisions in the middle west which defaulted during the 1870's and 1880's and settled with their creditors demonstrates this statement.

That the act operates to deprive non-consenting creditors of the right to enforce the levy of taxes without limit under writs of mandamus issued, does not interfere with the *State's power of taxation* or control of local fiscal affairs. It operates only to limit the remedies of creditors; it merely enforces the will of a majority of the creditors upon the dissenting minority. We call attention to sub-section (i), Section 83, to substantiate the fact that the statute does no interfere with the governmental powers of a local subdivision.

Approval of a composition under the present act, unless the dissenting creditors make it appear that the debtor's consenting creditors have received special consideration or, that the plan discriminates unfairly against a group or a class, or destroys liens or other vested rights, will operate in substantially the same way that Sec. 30, Title 11, operates.

The acceptance of the plan by a majority gives to the proceeding prima facie support of its fairness and confirmation merely enforces the contract between the majority creditors and the debtor against the dissenting minority in order to protect the debtor in its efforts to reestablish its credit and maintain the functions of government which it is obliged to perform for the benefit of its citizens under the State's grant of power to it.

The fear expressed in the majority opinion in the Ashton case that the act might be amended to provide for involuntary proceedings is not justified now if the former decision of this court is adhered to. An involuntary proceeding would unquestionably interfere with the State and taxing districts' independence. The mere fact that the Federal Courts have held that in the absence of a statutory grant they have power by writs of mandamus to compel taxing districts to levy taxes to pay judgments rendered against them is of itself a sufficient reason to justify Congress eliminating the use of such power where the majority of the creditors prefer to agree upon a method which will provide for orderly liquidation of debts. Acceptance of the consideration, if in new securities, does not give to creditors remedies which they would otherwise not possess. For the enforcement of them they must look to the remedies authorized by law at the time that they are issued. The assumption of jurisdiction by the court and its approval of the composition does not extend its power to enforce the new securities. This has been repeatedly held by Federal Courts under Section 30. Final decree of confirmation and distribution of the securities terminates the jurisdiction of the court. Thereafter the creditors all relegated in the event of future default or breach of the new contracts to their remedies in other forums.

Cary D. Landis

CARY D. LANDIS,
Attorney General of Florida.

Giles J. Patterson

GILES J. PATTERSON,
Special Counsel.